United States
Department of
Agriculture

Rural Business–
Cooperative
Service

USDA

Top 100 Cooperatives 1996 Financial Profile

Reprinted from *Rural Cooperatives* magazine,
September—December 1997

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Leveraging the Future? Higher Debt Levels Among Large Ag Co-ops May Be Cause for Concern

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Record Gross Revenues Do Not Translate Into Higher Net Margins for Largest Co-ops

David S. Chesnick

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Editor's Note: This is the first of three articles which provide an overview of how the nation's 100 largest agricultural cooperatives (based on gross sales) performed in 1996. Parts II and III follow on successive pages.

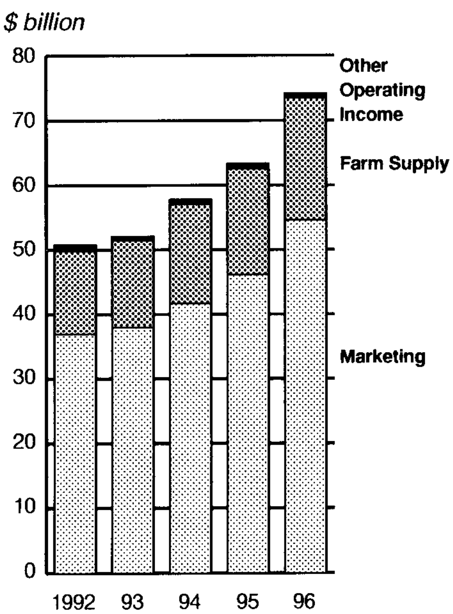
The nation's 100 largest agricultural cooperatives reported record revenues for the second year in a row in 1996. Operating revenues totaled more than $74 billion, up nearly $11 billion from the 1995 record (figure 1). However, net margins for the year were down.

Strategic alliances, higher grain prices and increases in value-added processing by cooperatives were major contributors to the rise in revenues. However, 52 percent of that increase was realized by just two cooperatives — Farmland Industries Inc., Kansas City, Mo., and Harvest States Cooperatives, St. Paul, Minn. They represented nearly a quarter of total operating revenue for the 100 largest co-ops, up from 20 percent in 1995.

Marketing sales continue to show tremendous gains, increasing more than 18 percent, to $55 billion, from the $46 billion recorded in 1995. This increase doubles the gain made the previous year. While three-quarters of the cooperatives that market their members' products had higher sales in 1996 than in 1995, 75 percent of the gain was generated by just 10 cooperatives. Grain sales accounted for about 65 percent of the total increase, followed by milk sales, which accounted for about 20 percent of the increase.

Farm supply cooperatives enjoyed substantial sales gains in 1996, following a year of relatively small gains in 1995. Farm supply sales rose 15 percent, to nearly $19 billion. However, 70 percent of that gain was due to five cooperatives. Sales increased for nearly every category of farm supplies, with 85 percent of the increase attributed to higher feed, fertilizer and petroleum sales.

Figure 1 — **Sources of Total Revenue**



Prior years restated

Table 1— **Consolidated statement of operations, 1995-96, top 100 cooperatives**

Operating statement	1996	1995	Difference	Percent Change
	---- Thousand Dollars ----			
Revenues				
Marketing	54,631,508	46,224,113	8,407,395	18.2
Farm Supply	18,933,572	16,421,488	2,512,084	15.3
Total Sales	73,565,080	62,645,601	10,919,479	17.4
Other Operating Revenues	711,369	757,852	(46,483)	–6.1
Total Operating Revenues	74,276,449	63,403,453	10,872,996	17.1
Cost of Goods Sold	67,438,087	56,607,951	10,830,136	19.1
Gross Margin	6,838,362	6,795,502	42,860	0.6
Expenses				
Operating Expenses	5,355,551	5,140,926	214,625	4.2
Net Operating Margins	1,482,811	1,654,576	(171,765)	–10.4
Other Revenues (Expenses)				
Interest Expense	(591,013)	(499,804)	(91,209)	18.2
Interest Revenue	99,626	103,925	(4,299)	–4.1
Other Income	186,086	129,476	56,610	43.7
Other Expenses	(31,329)	(33,185)	1,856	–5.6
Patronage Revenue	162,153	139,757	22,396	16.0
Net Margins from Operations	1,308,334	1,494,745	(186,411)	–12.5
Non-Operating Revenue (Expenses)	5,450	2,881	2,569	89.2
Net Margins	1,313,784	1,497,626	(183,842)	–12.3
Distribution of Net Margins				
Cash Patronage Dividends	338,204	435,972	(97,768)	–22.4
Retain Patronage Dividends	620,607	628,829	(8,222)	–1.3
Nonqualified Noncash Patronage	43,644	28,821	14,823	51.4
Dividends	26,833	23,090	3,743	16.2
Unallocated Equity	170,330	240,291	(69,961)	–29.1
Income Tax	114,166	140,623	(26,457)	–18.8
Total Distribution	1,313,784	1,497,626	(183,842)	–12.3

Other operating revenues were down nearly $46 million. These revenues are generally earned from services (such as storage, handling, spreading and other services provided to members). Although service revenue contributes an average of only 1 percent of total operating revenues, some cooperatives rely heavily on service revenue to boost their bottom line. For example, one cooperative received more than 35 percent of its operating revenue from receipts for services.

Cost of goods sold increased $10.8 billion in 1996, up 1 percent from 1995. This gain nearly surpassed the increase in total operating revenues, due most likely to increases in grain prices paid to members. However, substantial increase in farm supply sales, which carry higher margins, should have produced a relatively smaller increase in the cost of goods sold.

Operating expenses rose nearly 4.5 percent, to $5.4 billion, largely reflecting increased labor costs. Labor statistics obtained from 44 of the largest agricultural cooperatives showed labor expenses increased 7.5 percent from the previous year. If this sample is representative of the population, nearly 60 percent of the increase in operating expenses will be attributed to labor expenses.

Despite increased operating expenses, mergers and consolidation among cooperatives in the past few years have helped streamline their operations. For example, operating expenses as a percent of total sales continue to show small declines in each of the past 5 years. In 1992, total operating expenses consumed 11 percent of total revenues. By 1996, this ratio was down to 7 percent. This would imply that cooperatives are continuing to improve on the use of their resources.

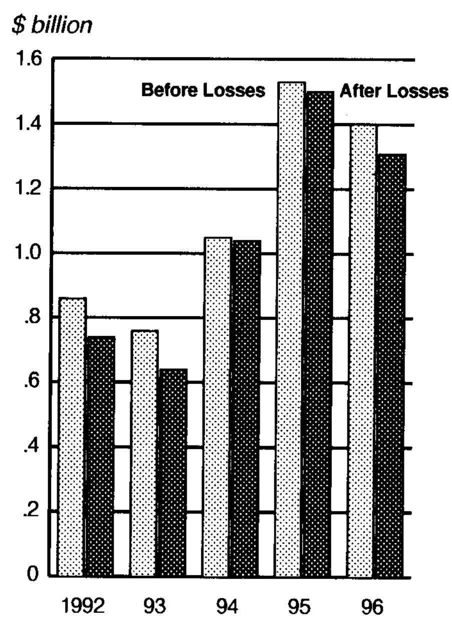
Other Income and Expenses

Income and expenses not directly related to the day-to-day operations fall into the category of "other income and expenses." These include patronage refunds received from other cooperatives, interest income and expense, gain/loss on the sale of equipment, and any other income/expense not related directly to operations. These expenses often relate to financing and investing activities of the cooperative.

Increased debt by cooperatives pushed up their interest expenses. Interest expense jumped 18 percent, or $91 million, to a record $591 million in 1996. This marks the third year in a row for double-digit increases in interest payments. On the other hand, interest revenue dropped 4 percent from a high of $103 million in 1995.

Patronage refunds (cash and non-cash) received from other cooperatives climbed 16 percent. Of the $162 million in patronage refunds, 27 percent was in cash. The rest were allocated non-cash patronage refunds. Seven cooperatives would have had an operating loss without patronage refunds.

Figure 2— **Net Margins/Losses**



Prior years restated

Net Margins

In 1996, net margins before taxes and extraordinary items were $1.3 billion. This is down 12.5 percent from the 1995 record. Higher cost of goods sold and labor expenses were the main reasons for the lower margins. Despite the decline, net margins from operations still posted the second highest level since USDA began tracking the largest agricultural cooperatives.

One cause for the drop in net margins was the number of cooperatives suffering losses during 1996. Nine cooperatives ended 1996 with a loss, up from six co-ops in 1995. Net margins before losses were $1.4 billion in 1996 (figure 2). Losses amounted to $86.6 million. However, 73 percent of the loss was attributed to one cooperative.

Non-operating Revenue

Non-operating revenues include gains or losses from discontinued operations, accounting changes and other extraordinary revenue or expenses not associated with operations. In 1996, these revenue sources reached $5.5 million, up 90 percent from 1995. However, that was not enough to boost net margins above 1995 levels.

Distributions of Net Margins

Cooperatives not only had fewer margins to distribute in 1996, but also paid out less cash as a percentage of total margins allocated (figures 3 and 4). In 1995, the largest agricultural cooperatives paid out $436 million (30 percent) of allocated equity in cash. By 1996, this figure was down to $338 million (26 percent).

The value of non-cash qualified patronage refunds declined from $629 million in 1995 to $621 million in 1996, a drop of 1 percent. But, as a percent of total distribution, cooperatives retained a higher percentage of their patronage refunds in 1996 (47 percent) than in 1995 (42 percent).

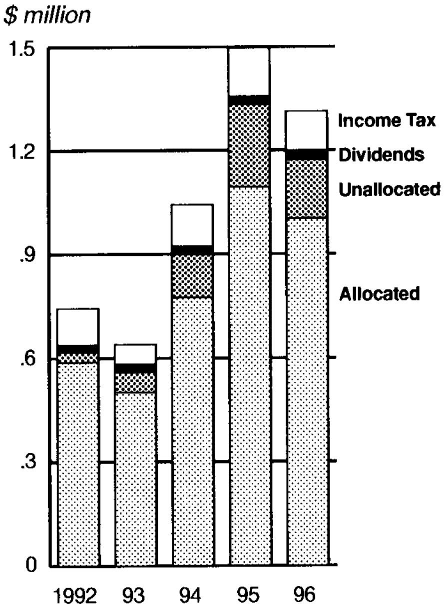
Although non-qualified non-cash patronage refunds represent 3.3 percent of total net margin distribution, the value jumped 50 percent, to $44 million, between 1995 and 1996. However, most of the increase was due to a single cooperative. Although these non-qualified patronage refunds add flexibility to the distribution mix, they are slowly losing favor with cooperatives. In the 1980s as many as 15 cooperatives used this form of allocation, but the number dropped to six co-ops in 1996.

Whether by regulation or cooperative policy, dividends usually play a minor role in distributing cooperatives' net income. However, the amount of dividends paid has increased in recent years. Before 1992, the average amount of dividends paid ranged between $13 million and $18 million. Since 1992, that amount has steadily increased, from $20 million to $27 million in 1996. Dividends paid on stock investment differs from patronage dividends or patronage refunds, which are based on the amount of business done with the cooperative.

Generally, unallocated equity or retained earnings are accumulated from non-member business. In 1996, unallocated equity levels declined. Cooperatives retained nearly 30 percent less of their earning than in 1995. This marks an abrupt change in the trend over the past five years. In 1992, the largest cooperatives retained $29 million. By 1995, this value stood at $240 million and in 1996 it dropped to $170 million.

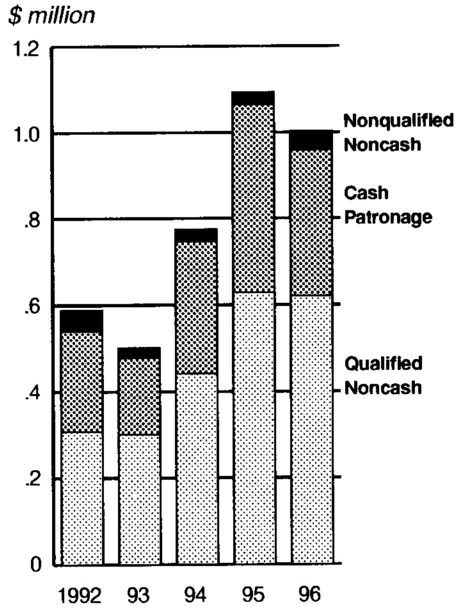
Even though cooperatives have a special tax status, they still pay income taxes. In 1996, cooperatives paid more than $114 million in income taxes, 19 percent less than in 1995. As a percent of net margins, the largest agricultural cooperatives paid an average tax rate of 9 percent, unchanged from 1995.

Figure 3 — **Distribution of Net Income**



Prior years restated

Figure 4 — **Patronage Refunds**



Prior years restated

Table 2— **Total revenue by commodity group, 1995-96, top 100 cooperatives**

Total revenue	1996	1995	Difference	Percent Change
	---- Thousand Dollars ----			
Cotton	2,346,263	2,694,323	(348,060)	–12.9
Dairy	18,460,584	16,707,931	1,752,653	10.5
Diversified	17,120,864	13,780,646	3,340,218	24.2
Fruit & Vegetable	7,473,799	7,101,667	372,132	5.2
Farm supply	9,193,881	8,137,604	1,056,277	13.0
Grain	16,390,219	11,635,134	4,755,085	40.9
Poultry & Livestock	1,122,000	1,175,679	(53,679)	–4.6
Rice	1,108,834	1,157,156	(48,322)	–4.2
Sugar	1,060,005	1,013,313	46,692	4.6

Table 3— **Net margins by commodity group, 1995-96, top 100 cooperatives**

Net margins	1996	1995	Difference	Percent Change
	---- Thousand Dollars ----			
Cotton	70,862	64,691	6,171	9.5
Dairy	216,559	190,661	25,898	13.6
Diversified	365,339	339,809	25,530	7.5
Fruit & Vegetable	14,441	143,646	(129,205)	–89.9
Farm Supply	558,024	506,655	51,369	10.1
Grain	76,037	249,539	(173,502)	–69.5
Poultry & Livestock	1,317	355	962	271.0
Rice	11,029	10,211	818	8.0
Sugar	2,812	(7,941)	10,753	*

* Cannot take percentage increase from a negative base.

Revenues by Commodity Group

In 1996, three commodity groups had lower sales than in 1995 (table 2). However, the drop in sales for these three cooperatives (cotton, poultry & livestock and rice) was overshadowed by the tremendous gains made by the other commodity groups. The biggest gainers were grain, diversified, dairy and farm supply cooperatives. However, the drop in net margins for grain and fruit & vegetable cooperatives more than offset the gains made by the other commodity groups, resulting in lower net margins for all cooperatives (table 3).

Grain cooperatives had the largest increase in sales, up 41 percent to $16.4

billion. The average prices for all grains in 1996 neared record levels. However, the high prices also pushed up payments to members and caused gross margins to drop 10 percent, to $593 million. Operating expenses increased 20 percent, to $492 million, half of which was due to higher labor costs. Consequently, net margins of $76 million were the lowest in the past five years.

The diversified cooperatives had the second highest increase in total revenues, up 25 percent, to $17 billion. Most of the increase was due to higher sales for grain (up 53 percent) and livestock (up 19 percent). Operating expenses increased a modest 5 percent while net margins rose 8 percent, to $365 million.

Due to a combination of higher prices and larger quantities, total revenues for dairy cooperatives hit $18.5 billion, up 10 percent from 1995. However, higher prices also pushed up cost of goods sold by 12 percent, to $1.8 billion. This lowered gross margins by 4 percent. Despite higher labor costs, dairy cooperatives cut operating expenses by 5 percent, thereby minimizing the effect of lower gross margins. Operating income was off only 1 percent from 1995. The $22 million increase in patronage refunds from other cooperatives helped push net margins up 12 percent to $214 million.

Farm supplies had another good year. Total revenues are up 13 percent, or $1 billion, reaching $9.1 billion. Even though cost of goods sold and operating expenses each increased by 8 percent, net margins reached the highest level to date. At $558 million, farm supply cooperatives also had the highest net margins of all commodity groups.

After two years of net losses as a commodity group, sugar cooperatives finally turned their operations around, posting $2.8 million in net margins. Although sales and gross margins have been increasing during the past five years, expenses increased faster. In 1996, the rate of increase for expenses slowed to 12 percent. Consequently, net operating margins increased 19 percent, to $14 million. Sugar cooperatives also had a 20 percent decease in interest expense which lead to the first positive net margins in the past three years.

Total revenue dropped for three commodity groups: rice, cotton, and poultry & livestock. Yet, all showed increases on their bottom line.

Rice cooperative revenues dropped 4 percent during 1996 while gross margins were down $14 million. However, this group was able to cut expenses by 7 percent, or $21 million, ultimately resulting in an 8-percent increase in net margins, to $11 million.

Cotton cooperatives faced a different situation. In 1996, cotton prices and volume were less than in 1995. Revenues dropped 13 percent in 1996 to $2.3 billion. However, cost of goods sold declined by 14 percent, to $2.1 billion. This combination caused gross margins to increase 5 percent, to $211 million. The cotton cooperatives held operating expenses to a 1-percent increase. Net margins increased 10 percent to $71 million — the highest amount since USDA began tracking the largest agricultural cooperatives.

While revenues and cost of goods sold both dropped 5 percent for poultry & livestock cooperatives, gross and net operating margins remained virtually unchanged. However, the poultry & livestock cooperatives continued to lose money on operations. Net operating losses were $6 million in 1996 and 1995. Yet, interest and other income were enough to offset operating losses in 1996, thereby pushing net margins to $1.3 million compared with $0.4 million in 1995. ■

Continued Expansion of Assets Shows Greater Reliance On Debt by Farmer Co-ops

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Editor's note: This is the second of three articles. The last article in the series follows this one.

The balance sheets of the nation's 100 largest cooperatives show that they continued to experience significant growth in 1996, although not quite as dramatic as the growth spurt seen in 1995 (figure 1). The rate of growth in combined assets was nearly 9 percent in 1996, down from 15 percent in 1995, but still is a strong indicator of economic health for the nation's largest cooperatives.

The balance sheet certainly does not tell all, but it does provide a good snapshot of the overall financial strength of the business at one point in time. The assets side of the balance sheet presents all the resources that the cooperative has invested. The other side indicates the sources from which these invested funds were financed. In other words, we see what the cooperative owns and who lays claim to these assets.

Total combined assets for the top 100 U.S. agricultural cooperatives stood at $25.6 billion in 1996, a $2-billion increase from 1995. The diversified and grain cooperative groups recorded the largest gains. Nearly two-thirds of the total combined increases in total assets were attributed to these two commodity groups. This expansion was fueled by higher levels of debt. Both short-term and long-term debt together increased 13.4 percent while total equity increased by only 7.5 percent (table 1).

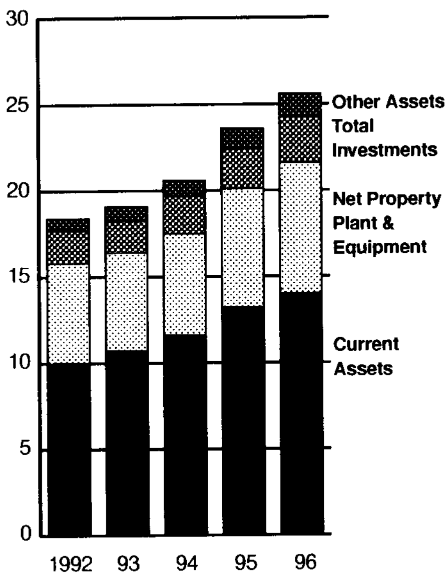
Current Assets Climb Slightly

While the growth of total assets in 1995 was fueled by the expansion of current assets, the growth of current assets in 1996 lagged behind growth in total assets. Current assets (comprised of cash, accounts receivable, inventory and "other" current assets) showed a modest gain of 6 percent, to $14 billion, when compared to 1995's growth rate of 14 percent. The percent of total assets represented by current assets declined from 56.1 percent in 1995 to 54.7 percent in 1996.

Most of the gains in current assets were in the form of inventory and accounts receivable (figure 2). Cash balances declined $60 million, to $850 million, by the end of 1996. That represents a 6.5-percent drop from 1995. Although dairy, fruit & vegetable and grain cooperatives increased their cash position, it was not enough to overcome the decline registered by all other commodity groups.

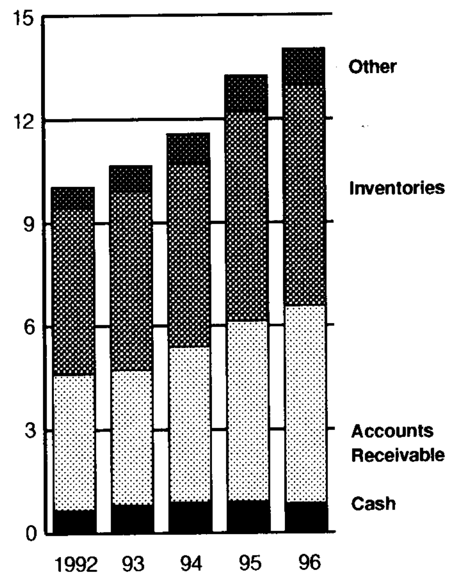
Accounts receivable ended the year at $5.7 billion, a $497 million (9.5 percent) increase, the largest gain in current assets. This increase in accounts receivable was proportional to the increase in sales in 1996. Nearly half of this increase can be attributed to diversified cooperatives with

Figure 1 — **Asset Composition, Top 100 Cooperatives, 1992–96**



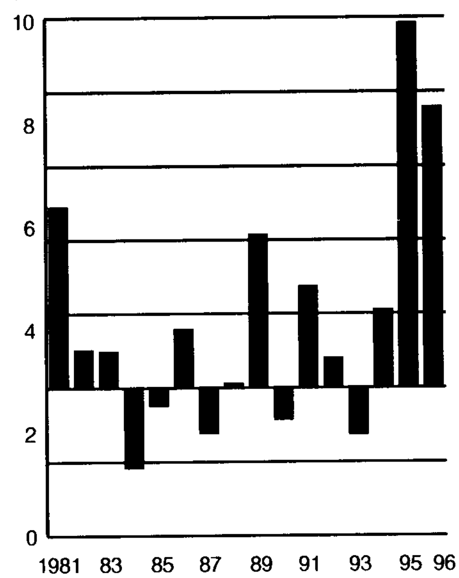
Prior years restated

Figure 2 — **Combined Current Assets, Top 100 Cooperatives, 1992–96**



Prior years restated

Figure 3 — **Yearly Change in Fixed Asset Investment, 1981–96**



Prior years restated

Table 1— **Combined balance sheet—Top 100, 1995-96**

Assets	1996	1995	Difference	% Change
		thousand $		
Current Assets				
Cash	849,857	908,920	(59,063)	(6.50)
Accounts Receivable	5,716,496	5,219,664	496,832	9.52
Inventory	6,413,999	6,082,713	331,286	5.45
Other Current Assets	1,040,453	1,030,300	10,153	0.99
Total Current Assets	14,020,805	13,241,597	779,208	5.88
Investment				
Bank of Cooperatives	435,016	408,031	26,985	6.61
Other Cooperatives	1,475,156	1,184,458	290,698	24.54
Other Investments	773,445	699,343	74,102	10.60
Total Investments	2,683,617	2,291,832	391,785	17.09
Net PP&E	7,638,136	6,879,190	758,946	11.03
Other Assets	1,302,491	1,195,849	106,642	8.92
Total Assets	25,645,049	23,608,468	2,036,581	8.63
Current Liabilities				
Short-term Debt				
Current Portion of Long-term Debt	898,788	406,921	491,867	120.88
Banks for Cooperatives	1,897,484	1,846,247	51,237	2.78
Commercial Banks	728,987	626,882	102,105	16.29
Notes Issued by Cooperatives	322,651	261,739	60,912	23.27
Other Nonfinancial Entities	27,047	24,394	2,653	10.88
Commercial Paper	108,699	147,767	(39,068)	(26.44)
Government Sources	44,981	27,464	17,517	63.78
Other Sources	5,436	4,459	977	21.91
Total Short-term Debt	4,034,073	3,345,873	688,200	20.57
Accounts Payable	3,497,859	3,176,943	320,916	10.10
Member Payables	403,939	478,747	(74,808)	(15.63)
Patron and Pool Liabilities	1,436,920	1,531,972	(95,052)	(6.20)
Other Current Liabilities	1,632,793	1,505,034	127,759	8.49
Total Current Liabilities	11,005,584	10,038,569	967,015	9.63
Long-term Debt				
Bank for Cooperatives	2,729,007	2,445,978	283,029	11.57
Bond Issued by Cooperative	1,295,591	1,069,879	225,712	21.10
Commercial Banks	683,878	395,416	288,462	72.95
Insurance Companies	419,225	445,643	(26,418)	(5.93)
Industrial Development Bonds	196,780	212,641	(15,861)	(7.46)
Capital Lease	57,702	54,460	3,242	5.95
Other Nonfinancial Entities	6,452	6,769	(317)	(4.68)
Government Source	1,064	930	134	14.41
Other Sources	208,797	128,304	80,493	62.74
Total Long-term Debt	5,598,496	4,760,020	838,476	17.61
Less Current Portion	4,699,708	4,353,099	346,609	7.96
Other Liabilities and Deferred Credits	674,362	618,943	55,419	8.95
Total Noncurrent Liabilities	5,374,070	4,972,042	402,028	8.09
Total Liabilities	16,379,654	15,010,611	1,369,043	9.12
Minority Interest	227,034	187,745	39,289	20.93
Member Equity				
Preferred Stock	1,749,589	1,619,691	129,898	8.02
Common Stock	600,817	568,909	31,908	5.61
Equity Certificates and Credits	5,022,918	4,654,440	368,478	7.92
Unallocated Capital	1,665,037	1,567,072	97,965	6.25
Total Equity	9,038,361	8,410,112	628,249	7.47
Total Liabilities and Equity	25,645,049	23,608,468	2,036,581	8.63

farm supply and grain cooperatives accounting for most of the rest.

The next largest increase was in inventories, which climbed 5.4 percent in 1996. This increase of $331 million boosted the total to $6.4 billion. However, the increase in inventories did not keep up with the sales level. This could mean cooperatives do not expect to sustain the higher sales volume in 1997 or they are becoming more efficient with their inventory management. This is especially true with the diversified cooperatives, which had a 25-percent increase in revenues but only a .5-percent increase in inventory. Dairy, farm supply and grain co-ops — which had the largest increase in inventories — all had revenue increase as well. Cotton and rice cooperatives had elevated inventory levels but the revenues declined, which is cause for concern.

Investments Hit Record Highs

Cooperatives invest in both non-cooperative and cooperative ventures (table 2). Investment in non-cooperative businesses generally indicates investments in joint ventures or other for-profit subsidiaries. Investments in other cooperatives usually indicates business done with other cooperatives, including CoBank and St. Paul Bank for Cooperatives. Total investment increased 17.1 percent, to $1.9 billion, a new record that surpassed the previous mark of $1.6 billion set in 1984.

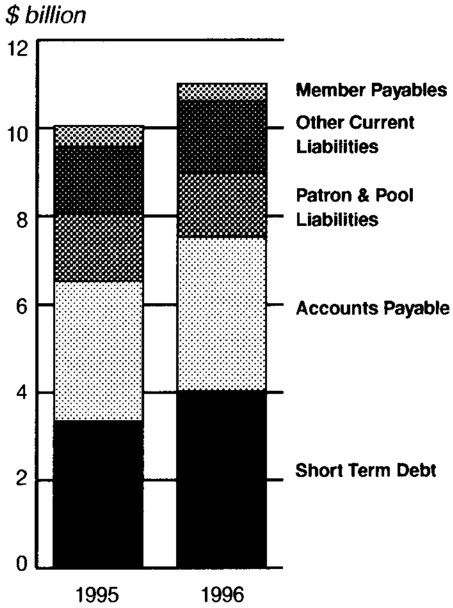
Cooperative investment in other cooperatives (excluding financial cooperatives) increased almost 25 percent, to $1.5 billion. Out of a total increase of $291 million, 70 percent reflected an ownership level of less than 20 percent and usually represents allocated non-cash patronage refunds. Diversified cooperatives provided the bulk of the increase with farm supply and grain cooperatives each contributing their share.

Investments that exceeded 20 percent ownership in other cooperatives increased 31 percent, to $87 million. When investments exceed 20 percent ownership, it usually represents joint ventures established to move more member products into the marketplace or to add value to the product. Leading the way in this area was the dairy cooperative group, which was responsible for 80 percent of the total increase.

Investment in financial cooperatives increased 6.6 percent, to $435 million. Grain cooperatives were the only commodity group that substantially increased their investments in financial cooperatives. The diversified and cotton cooperative groups each decreased their investment while the rest of the commodity groups were close to the overall average increase.

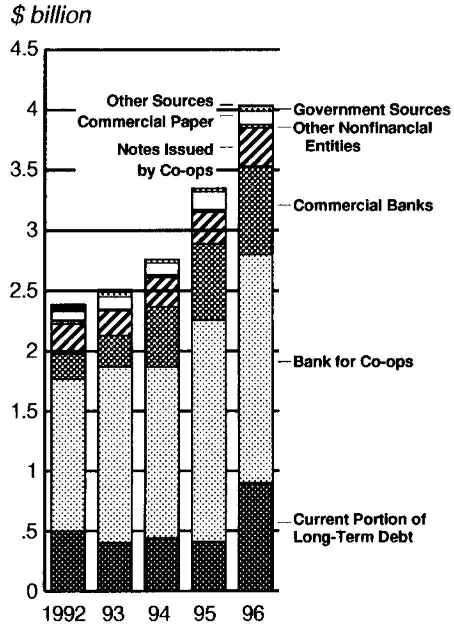
Investments in non-cooperative businesses increased 10.6 percent, to $773 million in 1996. This increase was stimulated mostly by a few diversified, grain and sugar cooperatives which invested in value-added businesses. Dairy cooperatives had a 50-percent drop in non-cooperative

Figure 5 — **Current Liabilities, Top 100 Cooperatives, 1995–96**



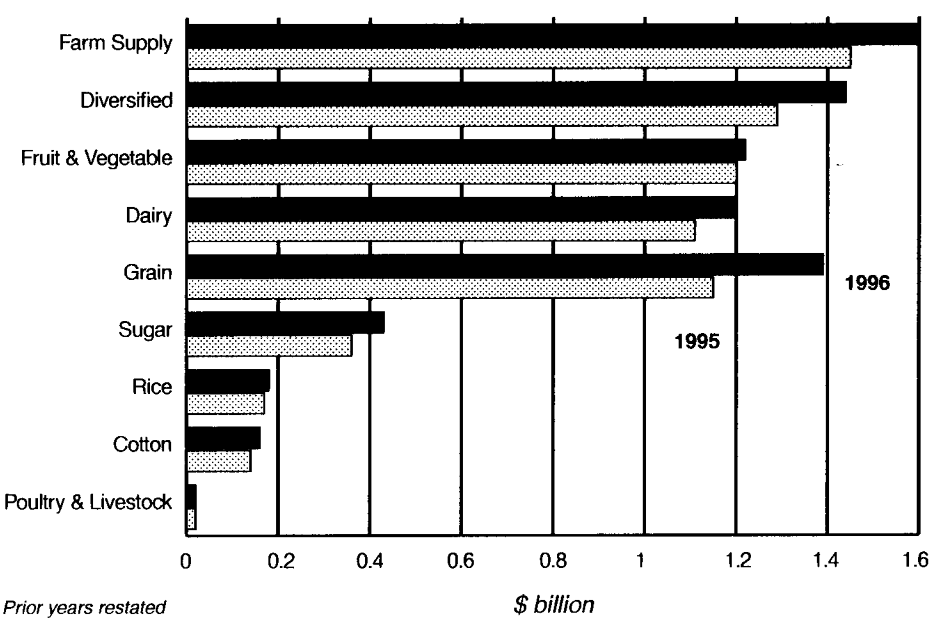
Prior years restated

Figure 6 — **Sources of Short-Term Debt, Top 100, 1992-96**



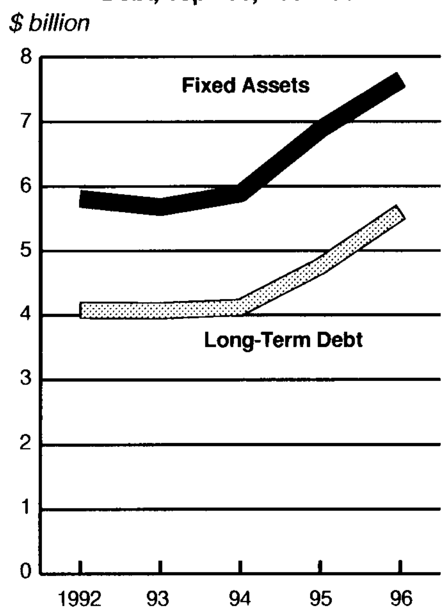
Prior years restated

Figure 4 — **Net Property, Plant, & Equipment, by Commodity Group**



Prior years restated

Figure 7 — **Fixed Assets and Long-Term Debt, Top 100, 1992–96**



Prior years restated